Postal Regulatory Commission
Submitted 6/10/2011 4:27:16 PM
Filing ID: 73205
Accepted 6/10/2011

UNITED STATES OF AMERICA
POSTAL REGULATORY COMMISSION
WASHINGTON, DC 20268-0001

Transferring Selected Post Office Box Service Locations to the Competitive Product List — Docket No. MC2011-25

PUBLIC REPRESENTATIVE COMMENTS ON
POSTAL SERVICE REQUEST TO TRANSFER
SELECTED POST OFFICE BOX SERVICE LOCATIONS
TO THE COMPETITIVE PRODUCT LIST

(June 10, 2011)

The Public Representative hereby provides comments pursuant to Order No. 732.[1] In that Order, the Commission established the above referenced docket to receive comments from interested persons, including the undersigned Public Representative, on the Postal Service's request to transfer Post Office Box (PO Box) service at approximately 6,800 locations from the market dominant product list to the competitive product list.[2] These locations, representing nearly one-fifth of all PO Box locations, are currently part of Post Office Box Service, a market dominant product in the Special Services class. If approved by the Commission, almost 49 percent of installed post office boxes and nearly 44 percent of all boxes in use by customers would be classified as competitive.[3]

Previously, in Docket No. MC2010-20, the Postal Service made its initial request to add a new product, Post Office Box service (Competitive), to the competitive product list.[4] As proposed, that new product would consist of PO Box service at 49 locations transferred from the market dominant product list.[5] The Commission approved this

[1] PRC Order 732, Notice and Order Concerning Request to Transfer Selected Post Office Box Service Locations to the Competitive Product List, May 18, 2011.
[2] Request of the United States Postal Service to Transfer Selected Post Office Box Service Locations to the Competitive Product List, May 13, 2011 (herein "Request").
[3] Request at 1-2, and fn. 5. The Postal Service's request does not propose to transfer Group E boxes.
[4] *See* Request of the United States Postal Service to Transfer Selected Post Office Box Service Locations to the Competitive Product List, Docket No. MC2010-20, March 12, 2010 (herein "Initial Request").
[5] Initial Request, Appendix D. Some PO Box locations have more than one ZIP Code. *Id.*, Appendix B, at 2, fn. 1.

initial request in Order No. 473.[6] At that time, the Postal Service also informed the Commission that it was evaluating all Post Office Box locations and would propose additional locations if warranted.[7] The instant request is an outgrowth of the Postal Service's completion of that evaluation.

In evaluating the Postal Service's request, the Commission is guided by 39 U.S.C. § 3642, which governs new products and transfers of products between the market dominant and competitive categories of mail. The first criterion in section 3642 to be considered when evaluating a request to add new products or transfer existing products is whether the Postal Service exercises sufficient market power

> that it can effectively set the price of such product substantially above costs, raise prices significantly, decrease quality, or decrease output, without risk of losing significant level of business to other firms offering similar products.[8]

Thus, for purposes of Commission evaluation of a transfer, section 3642(b)(1) establishes this central test for the existence of market power and, in this instance, places the burden on the Postal Service to refute the presumption that it exercises "sufficient" market power to justify its requested transfer.

For the reasons stated below, the Public Representative opposes the transfer of PO Box service at the 6,800 market dominant locations as the Postal Service's request in this docket fails to overcome this statutory presumption. The Public Representative's opposition is based upon available evidence and information presented by the Postal Service in this proceeding and in previous dockets, including MC2010-20, and MC96-3. Through a Motion, however, the Public Representative attempted to obtain additional information to permit a more thorough examination of the Postal Service's exercise of market power with respect to this expansion of competitive PO Box service, as required by 39 U.S.C. §3642.[9] For example, the Motion requested the sum total of installed boxes, occupied boxes, boxes eligible for renewal, boxes renewed by existing

[6] *See* PRC Order No. 473, Order Approving Request to Transfer Selected Post Office Box Service Locations to the Competitive Product List, Docket No. MC2010-20, June 17, 2010.
[7] Initial Request at 2.
[8] 39 U.S.C. §3642(b)(1). This criterion is also set-out in the Commission's rules at 39 C.F.R § 3020.32(d).
[9] *See* Public Representative Motion for Issuance of Information Request, June 1, 2011 (herein "Motion").

boxholders, and boxes rented by new boxholders for the months of October, November, and December 2010, and February, March and April 2011 for the 49 PO Box locations previously transferred.[10] If furnished, the requested data would allow an estimation of the price elasticity of demand for the competitive PO Box product. Nevertheless, given the available information, the Public Representative concludes that the Postal Service exercises sufficient market power such that it will be able to raise prices significantly and set the price of the approximately 6,800 additional locations proposed for transfer substantially above cost, without risk of losing a significant level of business to other firms offering similar products.

COMMENTS

On January 14, 2011, the Postal Service implemented a 25 percent price increase at the 49 PO Box locations previously transferred. Request, Attachment B, at 4. For these locations, the Postal Service reports a customer non-renewal rate for PO Box service of 31 percent during the three months (February – April 2011) following the price increase compared to an 11 percent non-renewal rate for the three months (October – December 2010) prior to the increase. *Id.* The Postal Service cites this data to assert that it is constrained from raising prices significantly. *Id.* Contrary to the Postal Service's assertion, however, data from the 25 percent price increase strongly suggests that the Postal Service can, without risk of losing a significant level of business to firms offering similar products, raise prices significantly, set prices substantially above cost, and decrease output.

The Postal Service's 25 percent price increase demonstrates its ability to raise prices significantly. In general, a 25 percent price in any truly competitive market would be met with some resistance, such as price matching by competitors or a price reduction or repeal by the initiating firm. For private mailbox (PMB) providers, there is no need to match the price increase as PMB prices are already higher because they offer a differentiated product, as discussed below. Most notably, the Postal Service

[10] *Id.*, Question 3(a).

makes no claim that its January 14, 2011, price increase has been reduced or repealed at any of the 49 PO Box locations. In fact, of the 31 percent of customers that did not renew PO Box service, the Postal Service was able to replace the 20 percent (31 percent – 11 percent) of customers that did not renew because of the price increase, as well as the 11 percent of customers that did not renew for other reasons. This fact demonstrates that the Postal Service has sufficient market power to raise prices significantly without risk of losing a significant level of business to other firms offering similar products. Moreover, the Public Representative submits that a price increase of 25 percent is a significant price increase as the cumulative rate of inflation during the period since enactment of the PAEA (January 2007 through April 2011) was 8.843% (219.0 / 201.9 – 1).[11]

The Postal Service's price increase (and the response thereto) also indicates that prices for PO Box service are relatively inelastic, which in turn suggests market (monopoly) power. For existing PO Box customers, the opportunity costs of not renewing service are relatively high, including: finding alternative box service; filing change-of-address or otherwise notifying family, friends and others of the change; and, for small businesses, the additional cost of changing stationery and the risk of lost remittances or sales because of the address change. Such opportunity costs are likely to far outweigh a PO Box price increase. At the same time, possible new customers must affirmatively act to obtain PO Box service—and pay for the delivery of mail that can be obtained for free from city delivery or rural carriers. Again, both the specific need for PO Box service, as well as the cost and effort required to obtain such service, suggests that the demand of possible new customers for PO Box service is relatively inelastic.

Moreover, the Postal Service's ability to "sign-up enough new customers to offset much of the increased rate of non-renewals,"[12] even in the face of a 25 percent price increase, reveals that the supply of available boxes is limited relative to the demand for boxes. The response to the price increase makes clear that the Postal Service has

[11] http://www.prc.gov/PRC-DOCS/home/CPI.pdf.
[12] Request, Appendix B at 9.

been able to effectively decrease output by constraining the number of post office boxes. There can be no other explanation for the Postal Service ability to replace most of the non-renewing customers with new customers.

Finally, approval of the Postal Service's request to transfer 6,800 PO Box locations would permit the Postal Service to set the price for this product substantially above cost. According to the Postal Service, transfer of these locations would result in an estimated cost coverage for the competitive PO Box service product of 143 percent. This compares to an estimated cost coverage for the market dominant PO Box service product of 113 percent.[13] A 25 percent price increase in which most non-renewing PO Box service customers are replaced by new customers would produce a substantially higher cost coverage for this competitive product. Under such circumstances, costs would not change, assuming there is no increase in installed/available boxes.[14] Based upon the Postal Service's cost analysis filed with its request, a 25 percent increase in the market dominant prices of post office boxes at the 6,800 locations proposed for transfer would result in a cost coverage of 178 percent.[15] .

Both the Postal Service and PMB providers agree that prices for PO Box service are generally lower than PMB prices.[16] The existence of prices for PO Box service lower than PMB prices explains the Postal Service's market power. The Postal Service states PMBs "offer the same basic service" and describes that basic service in *identical* terms to PO Box service: "a paid receptacle for the receipt of correspondence and packages." Request, Attachment B at 3. In addition to this most basic service, PO Box

[13] *See* Excel file POBoxServiceCostCoverage.xls, worksheet tab Cost Coverages. *See also* PRC Order No. 744, Order Concerning Analytical Principles Used in Periodic Reporting (Proposal One), Docket No. RM 2011-9, June 9, 2011, in which the Commission approved the change in methodology requested by the Postal Service whereby the attributable costs of Group E post office boxes would be treated as institutional rather than as part of the attributable costs of Post Office Box Service.

[14] PO Box costs are predominantly facility-related, *i.e.*, the sum of costs in Cost Segments 11, 15, 16 and 20. Such costs comprise 88 percent of total PO Box costs. *See* Excel file POBoxServiceCostCoverage.xls, worksheet tab Cost Flow Thru. However, replacing non-renewing customers with new customers would likely cause some increase in window clerk and supervisory costs.

[15] *See* Excel file POBoxServiceCostCoverage.xls, worksheet tab Cost Coverages. The 25 percent increase in revenues is calculated as follows: $455,426,691 * 1.25.

[16] Request, Appendix B at 8-9, citing Associated Mail & Parcel Centers Comments, Docket No. MC2010-20 (March 23, 2010); Mail & More of Tega Cay Comments, Docket No. MC2010-20 (March 31, 2010); National Alliance of Retail Ship Centers Comments, Docket No. MC2010-20 (March 31, 2010).

service and PMBs offer other common service features and attributes, including privacy and convenience. For such undifferentiated services features, PO Box service and PMBs are close substitutes and therefore should exhibit undifferentiated prices. However, the existence of different prices suggests that PO Box service and PMBs are differentiated products that serve the same market.

Importantly, it is the service features that differentiate these two products. In fact, PO Box service and PMBs offer unique service features or attributes that cannot be (or are not) matched by the other. For PO Box service, those features include a perceived greater level of security for remittances and high-value packages, as the Postal Service maintains custody of such items until the customer retrieves them, and generally earlier access to the mail at PO Box sections than PMBs, which rely on carrier delivery for receipt of mail that is then placed in the customer's mailbox.[17] For PMBs, the differentiating features include customer use of the PMBs street address, email notification by, or customer call-in to, the PMB concerning information on the receipt of correspondence or packages, and acceptance of packages from private carriers.[18]

The Postal Service's sole criterion for transferring the PO Box locations is proximity, using a "five mile metric" to identify so-called competitive PMBs. Request, Appendix B at 5. That metric focuses on the population within five miles of each PMB that is also served by a PO Box location. *Id.* As between a PO Box location and a PMB that are relatively close to the same population, proximity *per se* "does not reveal anything about the nature of the competition, if any, between post office boxes and [PMBs]".[19] In this instance, proximity is not a sufficiently compelling factor governing consumer choice that overrides all other service features distinguishing PO Box service from PMBs. Consequently, the Postal Service's focus on proximity is misleading for purposes of analyzing competition. Rather, PO Box service and PMBs should be analyzed as differentiated products serving the same market.

[17] Reply Brief of the United States Postal Service, Docket No. MC96-3, January 21, 1997, at 75.
[18] *See also* Comments of Associated Mail & Parcel Centers (AMPC), March 23, 2010 (Currently a dissimilar product, many PMB [Private Mail Box] locations enhance the mail receiving services by including email notification, street addresses, call-ins, free fax services, accepting private carrier packages, and store discounts among other services.)
[19] Public Representative Comments on Postal Service Request to Transfer Selected Post Office Box Service Locations to the Competitive Product List, Docket No. MC2010-20, March 31, 2010, at 2 (herein "Comments").

Despite its assertions in this case, Postal Service testimony supports the notion that PO Box service and PMBs are differentiated products serving the same market. In Docket No. MC96-3, the Postal Service describes the decision to obtain post office box service as a "binary" one—"you either have [box service] or you don't."[20]

> Because of the relatively low fees for post office boxes, the decision to obtain box service is not driven primarily by price, but by specific needs and by convenience. This is corroborated by the fact that so many people are willing to pay much higher fees for CMRA boxes.[21]

CONCLUSION

For the reasons stated above, the Public Representatives opposes the Postal Service's request to transfer the 6,800 PO Box locations to the competitive product list as the Postal Service is able to exercise sufficient market power with respect to PO Box service, and thereby fails the test in section 3642(b)(1).

The Public Representative respectfully submits the foregoing comments for the Commission's consideration.

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[20] Rebuttal Testimony of Paul M. Lion on Behalf of United States Postal Service (USPS-RT-3), Docket No. MC96-3, at 12. The Postal Service has provided no evidence to refute the sworn testimony of witness Lion. The acronym "CMRA" refers to Commercial Mail Receiving Agents," an alternative reference to PMBs.
[21] *Id.*